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No. 85-2142

In the Supreme Court of the United States

OCTOBER TERM, 1986

SOUTHWEST SUNSITES, INC., ET AL., PETITIONERS

v.

FEDERAL TRADE COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE FEDERAL TRADE COMMISSION IN OPPOSITION

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191

QUESTION PRESENTED

Whether the court of appeals correctly rejected petitioners' argument that the Federal Trade Commission's finding that they had engaged in "deceptive acts or practices" was based on a standard to which petitioners had no opportunity to respond.

TABLE OF CONTENTS

	Page
Opinions below	1
Jurisdiction	1
Statement	2
Argument	7
Conclusion	14

TABLE OF AUTHORITIES

Cases:

American Home Products Corp. v. *FTC*, 98 F.T.C. 136, aff'd, 695 F.2d 681 ..... 8, 11
Avnet, Inc. v. *FTC*, 511 F.2d 70, cert. denied, 423 U.S. 833 8
Bendix Corp. v. *FTC*, 450 F.2d 534 ..... 8, 9, 10
Bristol-Meyers Co., 85 F.T.C. 688 11
Cinderella Career & Finishing Schools, Inc. v. *FTC*, 425 F.2d 583 11-12
Cliffdale Associates, Inc., 103 F.T.C. 110 ..... 4, 5, 13
Crown Central Petroleum Corp., 84 F.T.C. 639 12
FTC v. *Colgate-Palmolive Co.*, 380 U.S. 374 12
FTC v. *Southwest Sunsites, Inc.*, No. CA 3-80-0258-F (N.D. Tex. May 19, 1980), aff'd in part and rev'd in part, 665 F.2d 711, cert. denied, 456 U.S. 973 4
FTC v. *Sperry & Hutchinson Co.*, 405 U.S. 233 ..... 10, 11
Firestone Tire & Rubber Co., 81 F.T.C. 389, aff'd, 481 F.2d 246, cert. denied, 414 U.S. 1112 ..... 11, 12
Ford Motor Co., 87 F.T.C. 756 12
Golden Grain Macaroni Co. v. *FTC*, 472 F.2d 882, cert. denied, 412 U.S. 918 8
Heinz W. Kirchner, 63 F.T.C. 1282 4
International Harvester Co., 104 F.T.C. 949 13
Kroger Co., 98 F.T.C. 639 12
L.G. Balfour Co. v. *FTC*, 442 F.2d 1 8

Cases—Continued: Page

NLRB v. *Mackay Radio & Telegraph Co.*, 304 U.S. 333 8
Rodale Press, Inc. v. *FTC*, 407 F.2d 1252 ..... 9, 10
Thompson Medical Co., 104 F.T.C. 648 13

Statutes:

Administrative Procedure Act, 5 U.S.C. 554(b) 6, 7
Federal Trade Commission Act, 15 U.S.C. (& Supp. II) 41 *et seq.*:
§ 5, 15 U.S.C. (& Supp. II) 45 ..... 3, 10, 11
§ 13(b), 15 U.S.C. 53(b) 3

Miscellaneous:

3 Trade Reg. Rep. (CCH) ¶ 22,251 (May 13, 1985) 3

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-12a) is reported at 785 F.2d 1431. The opinion and final order of the Federal Trade Commission (Pet. Supp. App. 1a-128a) and the initial decision of the administrative law judge are officially reported at 105 F.T.C. 7.

JURISDICTION

The judgment of the court of appeals was entered on April 1, 1986. The petition for a writ of certiorari was filed on June 30, 1986. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. Petitioners, three corporations and two individuals, acquired three large tracts of land in a sparsely-populated, semi-arid region of West Texas, subdivided the tracts into small parcels, and resold those unimproved parcels at per-acre prices that were 15 to 25 times higher than the prices petitioners had paid (Pet. App. 2a-3a; Pet. Supp. App. 24a-25a) and that "far exceeded the market value estimated by expert witnesses for both [the Federal Trade Commission and the petitioners]" (Pet. Supp. App. 46a). Petitioners marketed the property through a multimedia campaign consisting of television, radio, and newspaper advertising and in-home presentations that touted the investment potential of the land, as well as its suitability for homes, farming, and ranching (*id.* at 26a-29a, 36a-44a, 55a-58a). Petitioners also engaged real estate brokers, who sold the land by telephone nationwide and to residents of the island nations of the South Pacific. Petitioners supplied the brokers' salesmen with promotional literature and approved scripts for their telephone sales. *Id.* at 26a-32a, 97a-100a.

The central theme of petitioners' sales campaign was that the land was a "good, safe investment" (Pet. App. 2a). Buyers were told that "industrial development was likely" and that "[o]il, rubber, nuclear and uranium interests were all potential developments" (*id.* at 2a-3a). In fact, however, the evidence showed that the land was a poor investment. The selling prices of the parcels "were far greater than [their] fair market value" (Pet. Supp. App. 90a) and "there was virtually no resale market for the land" (*id.* at 47a). Moreover, the steep initial expenditures required to obtain utilities, water, and other amenities

rendered the land unsuitable for use as homesites or for farming (*id.* at 58a). Nor were the parcels suitable for small-scale ranching, because the "arid, semi-desert land is capable of supporting only six to ten head of cattle for each 640 acres of grazing area" (*id.* at 70a).

2. On April 29, 1980, the Federal Trade Commission (FTC) issued an administrative complaint alleging that petitioners' marketing techniques constituted unfair and deceptive acts and practices in violation of Section 5 of the Federal Trade Commission Act, 15 U.S.C. (& Supp. II) 45.[1] The complaint alleged that petitioners had (1) misrepresented that the undeveloped parcels were a good investment, involving little or no financial risk, and deceptively failed to disclose information concerning purchasers' financial risk; (2) misrepresented that the land was suitable for residential use, farming, and ranching, and deceptively failed to disclose material information regarding the suitability of the parcels for those purposes; and (3) sold land that was of little or no value for the purposes petitioners represented while unfairly retaining the proceeds from the sales (Pet. App. 3a; Pet. Supp. App. 23a-24a).[2]

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[1] The complaint also named one of petitioners' brokers, Porter Realty, Inc., and its president, Irvin Porter (Pet. Supp. App. 22a n.1), both of whom ultimately entered into consent agreements with the Commission. See 3 Trade Reg. Rep. (CCH) ¶ 22,251 (May 13, 1985).

[2] On April 9, 1980, the Commission, pursuant to Section 13(b) of the Federal Trade Commission Act, 15 U.S.C. 53(b), sought a preliminary injunction in the Northern District of Texas restraining petitioners' land sales practices pending final disposition of the administrative complaint. On May 19, 1981, the district court entered a preliminary injunction as to

On July 29, 1982, the administrative law judge filed an initial decision and order dismissing the complaint. Thereafter, on October 14, 1983, the Commission issued what has since been referred to as the Commission's "Deception Statement."[3] The Decep-

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the corporate petitioners, holding that the evidence demonstrated a likelihood that they had misrepresented and failed to disclose material facts concerning the investment potential and suitability of the land for the represented purposes. *FTC* v. *Southwest Sunsites, Inc.*, No. CA 3-80-0258-F (N.D. Tex.), slip op. 5. On the corporate petitioners' appeal, the United States Court of Appeals for the Fifth Circuit sustained the district court's grant of injunctive relief, holding that the evidence "suggests a large-scale systematic scheme tainted by fraudulent and deceptive practices." *FTC* v. *Southwest Sunsites, Inc.*, 665 F.2d 711, 723, cert. denied, 456 U.S. 973 (1982).

[3] The "Deception Statement" is actually a letter sent by the Commission to the Honorable John Dingell, Chairman of the Committee on Energy and Commerce of the House of Representatives, responding "to the Committee's inquiry regarding the Commission's enforcement policy against deceptive acts and practices" (*Cliffdale Associates, Inc.*, 103 F.T.C. 110, 174 (1984) (footnote omitted) (reprinting text of Deception Statement)). From past FTC and judicial decisions defining and elaborating the statutory phrase "deceptive acts or practices," the Commission identified three elements. The first element—that a representation, act or practice be "likely to mislead"—reflects what the Commission noted was the long-established principle that it need not find actual deception to hold that a violation has occurred. *Id.* at 176. The second element—that a representation, act or practice be considered from the perspective of the reasonable consumer—reflects according to the Commission a longstanding position that the law should not be applied so that honest representations are found deceptive merely because they can be " 'unreasonably misunderstood by an insignificant and unrepresentative segment of the class of persons to whom the representation is addressed' " (*id.* at 178, quoting *Heinz W. Kirchner*, 63 F.T.C.

tion Statement, adopted by the Commission in *Cliffdale Associates, Inc.*, 103 F.T.C. 110, 164-166, 176 (1984), provides that "[T]he Commission will find deception if there is a representation, omission or practice that is likely to mislead the consumer acting reasonably in the circumstances, to the consumer's detriment." See Pet. App. 4a.

On complaint counsel's appeal from the administrative law judge's (ALJ) decision, the Commission independently considered the entire record, including the initial decision and findings of the law judge, and, applying the articulation of "deceptive practices" contained in the Deception Statement, unanimously concluded that petitioners had engaged in unfair and deceptive conduct (Pet. Supp. App. 1a-128a).[4] The Commission held that petitioners had misrepresented the investment potential of the land and had deceptively failed to disclose the uncertainty of its f .ture value as well as the total absence of a resale market (*id.* at 45a-49a). Moreover, because of the steep costs of developing the arid land, the difficulties of climate, the problems of pest control and flooding, and the virtual absence of local markets, the Commission determined that the residential, farming, and ranching uses petitioners claimed for the land were wholly im-

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1282, 1290 (1963)). The last element—that a representation, act or practice be material—reflects the Commission's concern that the law be applied only against misinformation that is "important to consumers" and therefore "likely" to affect a consumer's choice of or conduct with respect to a product (103 F.T.C. at 182).

[4] While accepting most of the factual findings of the administrative law judge, the Commission rejected his determinations on liability because it concluded that the judge had misapprehended the allegations of the complaint (Pet. Supp. App. 41a-42a, 58a-59a).

practical (*id.* at 58a-71a). Finally, the Commission held that petitioners had engaged in "unfair practices" by deceptively inducing consumers to purchase land that had no value for the advertised uses and by using misrepresentations to induce purchasers to continue making payments on the parcels (*id.* at 94a-96a).

To remedy these violations of law, the Commission entered a cease and desist order that restricted petitioners' future sales activities. These restrictions required, among other things, that petitioners provide prospective buyers with information concerning the risks of purchase and include in future sales contracts specific buyers' rights (Pet. Supp. App. 114a-125a). The order also directed petitioners to send a letter to previous buyers, advising them of the Commission's findings (*id.* at 125a-127a).

3. The court of appeals affirmed (Pet. App. 1a-12a). It held, inter alia, that the Commission's factual findings were supported by substantial evidence (*id.* at 7a-11a) and that the cease and desist order was clearly within the Commission's remedial authority (*id.* at 12a). The court also rejected petitioners' argument that the Commission had violated due process and the Administrative Procedure Act (APA), 5 U.S.C. 554(b), by applying the allegedly narrower articulation of the meaning of "deceptive acts or practices" set forth in the "Deception Statement" (Pet. App. 4a-5a). The court said, "The purpose of the notice requirement in the Administrative Procedure Act is satisfied, and there is no due process violation, if the party proceeded against 'understood the issue' and 'was afforded full opportunity' to justify his conduct" (*id.* at 4a (citation omitted)). Applying that standard, the court held that "[t]his is

not a case in which" "a 'substantially different standard was applied, to which [petitioners] had no opportunity to respond' " or in which " 'different defenses and proofs would be used in defending against . . . two theories' of liability" (*id.* at 5a (citation omitted)).[5]

ARGUMENT

The court of appeals correctly rejected petitioners' due process and Administrative Procedure Act arguments. The court adopted what petitioners concede is the correct test: whether after the hearing before the administrative law judge "a substantially different standard was applied [by the agency], to which [petitioners] had no opportunity to respond" (Pet. App. 5a). The court correctly applied that test to the circumstances of this case, ruling that this was *not* a case where "different defenses and proofs would be used in defending against * * * two theories" (Pet. App. 5a): the complaint gave petitioners ample notice of the need to present any evidence and arguments they might have that their representations and practices were not likely to materially mislead reasonable consumers, and petitioners had a full opportunity to do so. There is no conflict with any decision of this Court or of another court of appeals, and review by this Court is not warranted.

1. Under the Administrative Procedure Act, 5 U.S.C. 554(b), any person who is otherwise entitled to notice of an administrative hearing must be informed of "the matters of fact and law asserted." But to satisfy the notice requirements of the APA and the Constitution, the agency need only give the

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[5] The court also rejected several other legal claims not presented in the petition (Pet. App. 5a-12a).

affected party a reasonable opportunity to know and meet the legal claims asserted. *NLRB* v. *Mackay Radio & Telegraph Co.*, 304 U.S. 333, 349-351 (1938); *Avnet, Inc.* v. *FTC*, 511 F.2d 70, 77 & n.18 (7th Cir.), cert. denied, 423 U.S. 833 (1975); *Golden Grain Macaroni Co.* v. *FTC*, 472 F.2d 882, 885-886 (9th Cir. 1972), cert. denied, 412 U.S. 918 (1973); *Bendix Corp.* v. *FTC*, 450 F.2d 534, 539-542 (6th Cir. 1971); *L.G. Balfour Co.* v. *FTC*, 442 F.2d 1, 19 (7th Cir. 1971). See also *American Home Products Corp.* v. *FTC*, 695 F.2d 681, 693-695 & n.21 (3d Cir. 1982). This is precisely the legal standard applied by the court of appeals. In rejecting petitioners' due process claim, the court held that "[t]he purpose of the notice requirement in the Administrative Procedure Act is satisfied, and there is no due process violation, if the party proceeded against 'understood the issue' and 'was afforded full opportunity' to justify his conduct" (Pet. App. 4a (citation omitted)). The court disagreed with petitioners only on the application of that standard to the circumstances of this case, determining that this was *not* a case in which " 'different defenses and proofs would be used in defending against . . . two theories' " (*ibid.*).[6]

2. The court of appeals' decision is entirely consistent with the decisions of the Sixth Circuit in

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[6] Petitioners err in relying on the court of appeals' observation (Pet. App. 5a) that "[a]ll evidence relevant to the old theory was necessarily relevant to the new" to show that the court applied some "novel 'relevance' test." The quoted observation plainly was not intended as the legal basis for the court's decision. The critical point is that petitioners failed to show that they had any evidence or argument that they did not present to the administrative law judge because it became relevant only under the Deception Statement articulation of the meaning of "deceptive acts or practices."

Bendix Corp. v. *FTC*, 450 F.2d 534 (1971), and the District of Columbia Circuit in *Rodale Press, Inc.* v. *FTC*, 407 F.2d 1252 (1968). Both of those cases involved the post-hearing adoption of an entirely new theory of liability, to which respondents had not had a fair opportunity to present defenses and proofs.

In *Bendix*, the Commission determined that an acquisition would lessen competition by eliminating the possibility that the acquiring company would instead enter the relevant market by making a so-called "toehold" acquisition; during the hearing, however, the Commission staff had relied on the quite different theory that the acquisition would eliminate the prospect that the acquiring company might enter the market by internal expansion (450 F.2d at 539-541). The court of appeals found that had the new theory been advanced earlier, respondent would have offered "different defenses and proofs" (*id.* at 541). Because "[t]he witnesses were questioned and cross-examined in terms of [the initial legal theory]" and "[t]he documentary proof was keyed to these theories," petitioner "was not accorded the opportunity to present proof and argument under the [new] theory of violation" (*id.* at 542).

In *Rodale Press*, the Commission ordered a publisher to cease placing particular advertisements promoting the sale of certain publications. The Commission found that the offending advertisements falsely represented that the publications would contain guaranteed cures for certain ailments when, in fact, the publications contained only qualified claims of cure. At the hearing, however, the parties had litigated on a quite different theory: that the advertisements correctly reported the contents of the publications, but that the cure-alls contained in the publications were

false. Judge Tamm, writing for the panel, held that this "change [of] theories in midstream" had deprived petitioners of "the *opportunity* to present argument under the new theory" (407 F.2d at 1256-1257 (emphasis in original)). Judge McGowan, joined by Judge Robinson, concurred, noting that the change in theories had denied the parties "an opportunity to defend, either by evidence or argument, against a charge *palpably different* from the one brought against them" (*id.* at 1258 (emphasis added)).

The court of appeals in this case applied the same standard as the Sixth and District of Columbia Circuits; the circuits are thus fully in accord on the governing principles. Here, as in those cases, the court inquired whether the new articulation of the meaning of "deceptive acts or practices" had effectively deprived petitioners of their opportunity to mount a defense. After examining the record, the court held that the application of the Deception Statement articulation did not abridge petitioners' full opportunity to defend "by evidence or argument" (*Rodale Press*, 407 F.2d at 1258 (McGowan, J., concurring)). Because the court of appeals applied the same standard as the courts in *Bendix* and *Rodale Press*, and merely concluded that under the circumstances of this case petitioners were *not* deprived of the opportunity to present relevant evidence or argument, there is no conflict and further review is unwarranted.[7]

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[7] This Court's decision in *FTC* v. *Sperry & Hutchinson Co.*, 405 U.S. 233 (1972)—on which petitioners also rely (Pet. 6-7)—simply does not address the issue posed in this case. There, the Court held that the Commission has the authority under Section 5 of the Federal Trade Commission Act to prohibit unfair methods of competition not otherwise forbidden by

3. Petitioners claim that there are two points on which, had they known that the Commission would apply the Deception Statement's articulation of the meaning of "deceptive practices," they would have offered different evidence or made different arguments. Both of these claims are plainly without merit.

Petitioners first argue that under "the new theory of deception * * * it would be relevant to survey consumers to determine the likelihood of deception" while "[u]nder the theory of deception at the time of the adjudication such evidence would have been irrelevant" (Pet. 7). But, first, petitioners ignore the fact that the Commission has long considered consumer surveys a valuable aid in determining the meaning of advertising. See, *e.g.*, *American Home Products Corp.*, 98 F.T.C. 136, 413-417 (1981), aff'd, 695 F.2d 681 (3d Cir. 1982); *Bristol-Meyers Co.*, 85 F.T.C. 688, 706-712, 744-745 (1975); *Firestone Tire & Rubber Co.*, 81 F.T.C. 398, 454-455 (1972), aff'd, 481 F.2d 246 (6th Cir.), cert. denied, 414 U.S. 1112 (1973). Indeed, the law is clear that when a party introduces extrinsic evidence on the meaning of advertising, the Commission must consider it. See *Cinderella Career & Finishing Schools, Inc.* v. *FTC*,

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the antitrust laws. However, because the Commission had predicated its order on a finding that the conduct in question *did* violate the antitrust laws—and had never relied on the broader Section 5 theory accepted by the Court—the Court was unable to uphold the order on its own terms. But the Court in *Sperry & Hutchinson* did not have any occasion to consider the standards that apply when a party asserts that its due process rights have been violated by a purported shift in an agency's legal theory.

425 F.2d 583, 585-589 & n.3 (D.C. Cir. 1970).[8] More important, the notion that petitioners had evidence that their advertising campaign was not "likely" to mislead, which they withheld because they thought the relevant standard was "tendency" to mislead, is neither plausible nor supported by any information either in the record or tendered to the court of appeals.

Equally mistaken is petitioners' contention (Pet. 8) that under the Deception Statement "evidence that the representations did not alter consumer behavior could have been decisive" while "[u]nder pre-existing law, it would have been unavailing for [petitioners] to have offered evidence that consumer decisions were not actually affected by the alleged representations." The Deception Statement does not suggest that practices must actually "alter consumer behavior" in order to be "deceptive." To the contrary, the Deception Statement states quite plainly, and consistently with prior policy, that "[t]he issue is whether the act or

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[8] Petitioners err in reading the Commission's decision in *Ford Motor Co.*, 87 F.T.C. 756, 794 (1976), to mean that survey evidence bearing on consumers' interpretation of challenged advertising is irrelevant under the previous definition of "deceptive practices" (Pet. 7). The *Ford Motor Co.* decision simply held that the Commission "is not required to survey public opinion" but may instead rely on its own " 'expertise * * * to interpret an advertisement' " (87 F.T.C. at 794, quoting *FTC* v. *Colgate-Palmolive Co.*, 380 U.S. 374, 391-392 (1965)). Moreover, any trace of ambiguity in *Ford Motor Co.* is dispelled by prior and subsequent decisions of the Commission recognizing that agency's duty to consider extrinsic evidence submitted by the parties. See, *e.g.*, *Cinderella Career & Finishing Schools, Inc.* v. *FTC*, *supra*; *Kroger Co.*, 98 F.T.C. 639, 728-729 & n.11 (1981); *Crown Central Petroleum Corp.*, 84 F.T.C. 1493, 1540 (1974); *Firestone Tire & Rubber Co.*, 81 F.T.C. at 454.

practice is likely to mislead, rather than whether it causes actual deception" (103 F.T.C. at 176 (footnote omitted)). Later FTC adjudicatory opinions applying the Deception Statement reaffirm that the Commission is concerned with the risk of consumer harm, not actual injury or reliance. See *International Harvester Co.*, 104 F.T.C. 949, 1056 (1984); *Thompson Medical Co.*, 104 F.T.C. 648, 816 (1984); *Cliffdale Associates, Inc.*, 103 F.T.C. at 165. Thus, petitioners' claim that the Deception Statement makes relevant their supposed evidence that consumers did not actually rely on their advertisements is based on a misreading of the Deception Statement.

4. Petitioners also suggest (Pet. 8 (emphasis in original)) that had the articulation in the Deception Statement been promulgated prior to the hearing petitioners would have seized "the opportunity to address the effect of the change on the *staff's* case," presumably by contending that the staff had failed to meet its "burden of proof." But petitioners do not identify how, if at all, the staff's proof failed to measure up under what they perceive as the new "burden of proof"; nor do they challenge the court of appeals' determination (Pet. App. 7a-11a) that the Commission's findings were supported by substantial evidence.

The Commission regards the Disclosure Statement as merely a synthesis of elements of prior case law. See, *e.g.*, 103 F.T.C. at 175 (citation omitted) ("We have therefore reviewed the decided cases to synthesize the most important principles of general applicability"); *id.* at 165 ("These elements articulate the factors actually used in most earlier Commission cases identifying whether or not an act or practice was deceptive * * *."). Petitioners' contention that they were found liable on a fundamentally new theory,

which they did not have a chance to rebut, is simply without merit.

Finally, petitioners argue (Pet. 8) that the application of the Deception Statement "denied [them] the right to have the issues * * * decided in the first instance by the ALJ who observed the witnesses." But the Commission accepted, for the most part, the ALJ's factual findings, disagreeing only with his understanding of the allegations of the Complaint. Moreover, petitioners fail to suggest how, if at all, a fresh look at the evidence would have altered the factual findings or outcome of the case.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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